

Initial Statement of Reasons  
Overview/Non-Controlling Summary

Regulation 1616, Federal Areas

Regulation 1616, “Federal Areas,” in part explains when Indian retailers selling tangible personal property on an Indian reservation must collect use tax from non-Indians and Indians who do not reside on a reservation.

Specific Purpose

The purpose of the proposed amendment is to interpret, implement, and make specific Revenue and Taxation Code Section 6352 as it applies to certain sales of tangible personal property on Indian reservations. This amendment is necessary to provide guidance to the taxpayers that engage in such transactions as to whether specific transactions are subject to tax.

Factual Basis

Regulation 1616 discusses the application of tax to sales of tangible personal property in areas owned or operated by the federal government or entities involved in federal operations. In part, it discusses sales by Indian retailers on the reservations to Indians who reside on the reservation, to Indians who reside off the reservation, or to non-Indians. Currently, the regulation provides that sales or leases of tangible personal property to non-Indians and Indians who do not reside on the reservation are fully subject to tax.

Regulation 1616(d)(3)(A)2. currently imposes the obligation to collect use tax on Indian retailers on their sales of tangible personal property to non-Indians and Indians who do not reside on the reservation.

The Board concluded, since Regulation 1616(d) was adopted in 1978, that federal courts have consistently held that if a tribal seller makes a specific investment in a product, has significant direct involvement in its sale to a non-member, and is otherwise adding real value to a product sold on the reservation, then federal law pre-empts the state’s jurisdiction to impose a use tax collection obligation on Indian retailers’ on-reservation sales of that product to a non-Indian or an Indian who does not reside on the reservation.<sup>1</sup> The Board concluded that these cases have called the validity of subdivision 1616(d)(3)(A)2. into question.

The Indian retailer’s obligation to collect use tax on the sale of meals, food and beverages to non-Indians and Indians who do not reside on a reservation has been the

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<sup>1</sup> See, e.g., *Washington v. Confederated Tribes of the Colville Indian Reservation* (1980) 447 U.S. 134, 156-157; *White Mountain Apache Tribe v. Bracker* (1980) 448 U.S. 136; *Ramah Navajo School Board, Inc. v. Bureau of Revenue of New Mexico* (1982) 458 U.S. 832; *New Mexico v. Mescalero Apache Tribe* (1983) 462 U.S. 324; *California v. Cabazon Band of Indians* (1987) 480 U.S. 202.

subject of recent hearings before the Board. In these cases, the purchaser does not bring the meals, food or beverages home for use, but instead purchases the meals, foods or beverage at an on-reservation eating and drinking establishment for consumption at the on-reservation eating and drinking establishment.

The proposed amendments concerning meals, food and beverages would exempt on-reservation Indian retailers from a duty to collect use tax on the sale of meals, food and beverages to non-Indians and Indians who do not reside on the reservation, when the meals, food and beverages are purchased for consumption at on-reservation eating and drinking establishments.

The Board considered that the proposed amendments to Regulation 1616 are exemptions pursuant to Revenue and Taxation Code section 6352, which provides that if the Constitution the Board from imposing tax, the Board may not impose such a tax: if there is no prohibition against tax, tax applies, and the Board requires a federal judicial decision or other authority, such as a statutory change, to exempt the application of tax.

The Board concluded that the amendments are consistent with federal law, express existing federal law with regard to states' ability to impose a duty to collect tax upon on-reservation Indian retailers, and would make Regulation 1616(d) conform to federal law.

The Board further concluded that, with regard to the sales of meals, food and beverages sold for consumption at on-reservation eating and drinking establishments, Regulation 1616(d)(3) should be revised to eliminate the requirement placed on Indian retailers to collect the use tax from non- Indian purchasers, and from Indian purchasers who do not reside on the reservation,

On March 27, 2002, the Board held a public hearing on proposed amendments to Regulation 1616, concerning sales of tangible personal property on Indian reservations. That same day, the Board adopted proposed amendments to Regulation 1616. The Rulemaking File was submitted to the Office of Administrative Law (OAL) in May of 2002. On June 18, 2002, in a facsimile transmission, OAL stated that the Rulemaking File as submitted could not be approved. OAL stated that it would reject the proposed amendments under the consistency and necessity standards (Government Code section 11349.1); that it would also reject proposed subdivision (d)(3)(A)2.b. individually under the clarity standard (Government Code section 11349.1); and that the Rulemaking File did not properly summarize and respond to the public comments. On July 16, 2002, the Board withdrew the proposed amendments to the regulation in lieu of OAL rejecting the proposed changes.

To resolve OAL's clarity objection, the Board deleted proposed subdivision (d)(3)(A)2.b. entirely. As a result of this deletion, the Board also moved the text of proposed subdivision (d)(3)(A)2.a, concerning meals, food, and beverages to subdivision (d)(3)(A)2. as a separate unnumbered paragraph. The Board adopted that

language on October 3, 2002 and re-submitted it to OAL.

In a further effort to craft a regulation which meets OAL's requirements and accomplish the original intent, the Board, on November 12, 2002, authorized for publication new amendments to the amended text.

The Board determined that federal law preempts the state from imposing a duty upon Indian retailers to collect use tax on the on-reservation sales of property intended for use in on-reservation gaming activities, or that promotes on-reservation gaming activities, as defined in the new proposed amendments, because of the pervasive federal regulation of Indian gaming by the Indian Gaming Regulatory Act (25 U.S.C. § 2701, et seq.).

The Board further determined that federal case law preempts the state from imposing a duty upon Indian retailers to collect use tax on the on-reservation sale to non-Indians and Indians who do not reside on the reservation, of tangible personal property in which the tribal seller has made a specific investment, has significant direct involvement in its sale to a non-member, and is otherwise adding real value to a product sold on the reservation.<sup>2</sup> The Board has determined that these conditions are fulfilled when the on-reservation retailer sells products which are made of raw materials produced on the reservation, are reflective of tribal culture, history or tradition, are intended to be used in an on-reservation activity, or generally cannot be purchased outside a reservation.

The Board considered that the new amendments to Regulation 1616 are exemptions pursuant to Revenue and Taxation Code section 6352, which provides that if the Constitution prohibits the Board from imposing tax, the Board may not impose such a tax: if there is no prohibition against tax, tax applies, and the Board requires a federal judicial decision or other authority, such as a statutory change, to exempt the application of tax.

The Board concluded that the new amendments are consistent with federal law, express existing federal law with regard to states' ability to impose a duty to collect tax upon on-reservation Indian retailers, and would make Regulation 1616(d) conform to federal law.

The Board has concluded that Regulation 1616(d)(3) should be revised to eliminate the requirement placed on Indian retailers to collect the use tax from non-Indians, and from Indians who do not reside on the reservation, when purchasing on the reservation tangible personal property that (1) is intended for use in on-reservation gaming, as defined; (2) promotes on-reservation gaming activities, as defined; (2) is made from raw materials produced on the reservation; (3) reflects tribal history, culture or tradition; (4) is intended for use in an on-reservation activity; or (5) is not generally available for purchase outside of a reservation

Subdivision (d)(3)(A)2. Phrase "or ... policy" added to third sentence. Designation "a." added to un-numbered paragraph. New subdivision (d)(3)(A)2.b. added to provide

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<sup>2</sup> See cases cited in footnote 1, above.

that Indian tribes are not required to collect use tax on the sale of tangible personal property sold on a reservation, without regard to the origin of such tangible personal property, if the tangible personal property is intended for use in relation to on-reservation gaming activities, as defined, or promotes on-reservation gaming activities, as defined. New subdivision (d)(3)(A)2.c. added to provide that Indian tribes/Indian retailers are not required to collect use tax on the sale of tangible personal property sold on a reservation if the property a) is made from raw materials produced on the reservation, b) reflects or illustrates tribal history, culture or tradition, c) is intended for use in an on-reservation activity, or d) is not generally available for purchase outside of a reservation.

Pursuant to Government Code section 11346.5(a)(8), the Board of Equalization finds that the adoption of the proposed amendments will not have a significant adverse economic impact on private businesses or persons. The amendments are proposed to interpret, implement, and make specific the authorizing statutes in the context covered by the regulation for greater ease of understanding and to conform the regulation to recent legislation. These changes will clarify the interpretation or administration of the sales and use tax laws. Therefore, the Board has determined that these changes will not have a significant adverse economic impact on private businesses or persons.

The new amendments exempt Indian retailers from the duty to collect use tax on the on-reservation sales of specific types of tangible personal property, to non-Indians and Indians who do not reside on the reservation.